



**KRAKEN ROBOTICS INC.
MANAGEMENT DISCUSSION AND ANALYSIS
FOR THE THREE MONTH PERIOD ENDING MARCH 31, 2021**

This Management Discussion and Analysis ("MD&A") of Kraken Robotics Inc. (the "Company" or "Kraken") provides analysis of the Company's financial results for the three month period ended March 31, 2021 and should be read in conjunction with the Company's audited financial statements and the notes thereto for year ended December 31, 2020, which are available on SEDAR at www.sedar.com. This MD&A is current as at May 26, 2021, the date of preparation.

The March 31, 2021 condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") applicable to the preparation of interim financial statements. These financial statements were prepared using the same accounting policies and methods of computation, and are subject to the same use of estimates and judgments, as the Company's consolidated financial statements for the year ended December 31, 2020. These condensed consolidated interim financial statements do not include all disclosures required by International Financial Reporting Standards ("IFRS") for annual consolidated financial statements and accordingly should be read in conjunction with the Company's audited consolidated financial statements for the year ended December 31, 2020 prepared in accordance with IFRS as issued by the International Accounting Standards Board ("IASB"). All amounts are expressed in Canadian dollars, unless otherwise stated.

Forward-Looking Statements

*This MD&A, and, in particular, the sections below entitled "Nature of Business", "Use of Estimates and Judgments", "Capital Management", "Financial Instruments and Risk Management" and "Risks and Uncertainties" contain "forward-looking statements" and "forward-looking information" (collectively, "**forward-looking statements**") within the meaning of applicable Canadian securities legislation.*

In some cases, forward-looking statements can be identified by the use of forward-looking terminology such as "may", "will", "expect", "intend", "seek", "potential", "estimate", "anticipate", "believe", "could", "would", "should", "continue", "plans", "target", "is/are likely to", or the negative of these terms, or similar expressions intended to identify forward-looking statements. Within this MD&A, forward-looking statements may include, without limitation, statements with respect to Kraken's future plans, strategies and objectives, including:

- *expectations regarding revenue, expenses and operations;*
- *the ability to execute on its contracts announced for products including: AquaPix® MINSAS, SeaVision® 3D laser system, KATFISH™, ThunderFish® AUV, ALARS, batteries and thruster products;*
- *anticipated cash needs and the Company's needs for, and the Company's ability to secure, additional financing and/or government funding for working capital needs, debt repayment obligations and other contractual obligations of the Company;*
- *the Company's ability to maintain current and projected revenue if it fails to effectively compete for additional contracts;*
- *our ability and intention to expand Robotics as a Service and data analytics revenue;*
- *our expectations respecting our OceanVision™ project for the development of new marine technologies and products to enable an underwater robotics data acquisition and data analytics as a service business;*
- *the Company's ability to protect, maintain and enforce its intellectual property rights;*
- *the Company's ability to defend itself against third-party claims of infringement or violation of, or other conflicts with, intellectual property rights by the Company;*
- *expectations regarding capital markets and the Company's ability to continue to obtain financing while markets are affected by the global COVID-19 pandemic;*
- *the Company's ability to attract new customers;*
- *the Company's ability to attract and retain personnel;*
- *the Company's competitive position and its expectations regarding competition and its future success in competitive bidding processes.*

Forward-looking statements reflect the Company's current views with respect to future events and are subject to various known and unknown risks and uncertainties, which are necessarily based upon a number of estimates and assumptions that, while considered reasonable by Kraken, are inherently beyond the ability of the Company to control or predict, that may cause the Company's actual results, performance or achievements to be materially different from those expressed or implied thereby, and are developed based on assumptions about such risks, uncertainties and other factors set out herein, including but not limited to the factors referred to below under "Risks and Uncertainties". For additional information with respect to certain of these risks or uncertainties, reference should be made to the section entitled "Risks and Uncertainties" in this MD&A and to Kraken's continuous disclosure materials filed from time to time with the Canadian Securities Regulatory Authorities, including the Company's Annual Information Form for the financial year ended December 31, 2020 under the section entitled "Risk Factors", quarterly and annual reports, and supplementary information, which are available on SEDAR at www.sedar.com. Additional risks and uncertainties not presently known to the Company or that Kraken believes to be less significant may also adversely affect the Company.

The Company undertakes no obligation to update forward-looking statements except as required by applicable law. Such forward-looking statements represent management's best judgment based on information currently available. No forward-looking statement can be guaranteed, and actual future results may vary materially. Accordingly, readers are cautioned not to place undue reliance on forward-looking statements.

NATURE OF BUSINESS

Kraken Robotics Inc. (formerly Kraken Sonar Inc.) was incorporated on May 14, 2008 under the Business Corporations Act, British Columbia, is a publicly traded company, and its registered office is at 100 King Street West, #1600, Toronto, Ontario, M5X 1G5.

The Company's principal business is the design, manufacture and sale of software centric sensors, batteries, and underwater robotic systems.

Company Overview

Kraken Robotics Inc. (PNG: TSX-V) is a marine technology company supplying advanced sonar and optical sensors, batteries, and underwater robotics equipment for military and commercial applications. The Company is recognized as world leading innovators of Synthetic Aperture Sonar (SAS) - a revolutionary underwater imaging technology that dramatically improves seabed surveys by providing ultra-high resolution imagery at superior coverage rates. Both military and commercial markets are showing encouraging growth as they are now incorporating unmanned vehicles and intelligent sensors in their procurement plans and budgets.

AQUAPIX® MINSAS SENSOR FOR UNDERWATER VEHICLES

The AquaPix® MINSAS (Miniature Interferometric Synthetic Aperture Sonar) sensor is based upon Kraken's core Synthetic Aperture Sonar technology. The MINSAS compact receiver array length of only 60cm recently improved the AquaPix® SAS image resolution from 3.0 x 3.3 cm (across along track) to an industry-leading 1.9 x 2.1 cm while maintaining a constant Ultra HD resolution across ranges up to 120M per side. The lightweight array is integrated into a modular payload section of less than eight-inch diameter, which can be easily mobilized in customers' Unmanned Underwater Vehicles (UUVs) of all sizes. The MINSAS payload section also includes Kraken's latest generation Real Time SAS Processor, the RTSAS MK-II. The RTSAS enables real-time, onboard processing of SAS imagery and bathymetry at full resolution and allows operators to leverage Kraken's suite of post-processing tools, including the newly developed SASView 3D sonar visualization and control software. The MINSAS plus RTSAS provides operators with an area coverage rate of higher than 3km² per hour at full SAS resolution, enabling highly efficient survey operations. Development continues our new Multispectral SAS product, this product will provide a unique capability, enabling simultaneous ultra-high-resolution acoustic imagery and buried object detection from the same sensor.

SEAVISION® 3D LASER SYSTEM FOR UNDERWATER VEHICLES

Kraken Robotik GmbH ("KRG"), a wholly-owned subsidiary of the Company, commenced operations in January 2017 in Bremen, Germany. Its focus is the development of 3D imaging sensors, machine learning, and artificial intelligence (AI) algorithms for underwater robotic platforms.

KRG, with support from Kraken engineers in Canada, has developed the SeaVision® 3D laser system. SeaVision® is the world's first RGB underwater laser imaging system that offers the resolution, range and scan rate to deliver dense full colour 3D point cloud images of subsea infrastructure with millimeter accuracy, in real time. The ability to generate accurate 3D reconstruction of underwater infrastructure is an important requirement for commercial, military and ocean research applications. The initial system is designed for deployment on underwater robotic platforms such as Remotely Operated Vehicles (ROVs) and AUVs. Kraken has seen significant interest in SeaVision® from customers across many industries from defense to oil and gas, to renewable energy and nuclear.

In collaboration with an international oil and gas company, Kraken's development of a unique, non-contact mooring chain inspection tool continues, with commercialization scheduled for the second half 2021. This tool, utilizing SeaVision® platform can be used to support existing offshore oil and gas inspection requirements, as well as upcoming offshore wind inspection requirements. This new platform is anticipated to significantly reduce the cost of inspecting critical infrastructure, which must be inspected regularly.

Kraken continues development of its SeaVision® laser profiler product which can be integrated on AUVs and tow bodies from Kraken and other manufacturers.

KATFISH™ TOWED UNDERWATER VEHICLE

Kraken has developed the Kraken Active Towed Fish (KATFISH™) for high speed, high resolution seabed mapping. The system enables real-time seabed imagery, bathymetry and advanced 3D digital terrain models of the seabed – optimized for both manned and unmanned surface vessels. Coupled with Kraken's revolutionary AquaPix® MINSAS, it is especially well-suited for both military and commercial seabed surveys.

In the commercial seabed survey market, KATFISH™ offers offshore energy companies the advantage of comprehensive, high-resolution surveys of existing infrastructure, such as pipelines and subsea stations, completed in at least half the time as more conventional methods. KATFISH™ operates at speeds up to 10 knots, versus the slow moving 1-2 knots of ROV or the medium 3-4 knots of the passively stable sonar systems, thus reducing operating time and cost.

In the defence market, there is a growing global requirement for modernization of mine countermeasure (MCM) solutions. The previous generation of single-role mine hunting vessels designed and built between the 1970's - 1990's are now being withdrawn from service. This leaves a growing requirement for high resolution, high speed seabed imaging platforms.

The ability of the KATFISH™ platform to generate centimetre-scale sonar resolution in all three dimensions can provide significant improvement in the detection, classification and identification of small seabed objects for both military and commercial seabed survey missions.

Kraken has high expectations for the KATFISH™ which provides high performance underwater mapping and mine hunting capabilities from a towed platform for both the military and commercial markets and expects it to be a key revenue driver for the Company. The Company has in the past and will in the future partner as a supplier to large defense contractors who are involved in various multi-unit bids.

Recent updates and developments with KATFISH™ include:

- In September 2020, Kraken secured a contract through a competitive bid process with the Danish Ministry of Defence, Acquisition and Logistics Organization to supply mine-hunting sonar equipment to the Royal Danish Navy. Under the program, Kraken will provide its mine-hunting KATFISH™ towed SAS system, the Tentacle® Winch system, and Autonomous Launch and Recovery System ("ALARS") to be integrated onboard the Royal Danish Navy's optionally unmanned surface vessels. The aggregate value of the contract is \$36 million, deliverable over a 5-to-10-year period, with the majority of funds (approximately \$22 million) to be received over the two-to-three-year product acquisition phase, with the remaining funds (approximately \$14 million) being allocated to post sales service arrangements which will continue for the duration of the remaining term.
- In September 2020, Kraken signed a contract for supply of mine-hunting systems to Remontowa Shipbuilding S.A., to be integrated on the Polish Navy's new KORMORAN II CounterMeasure (MCMV) vessels. It is expected that the equipment will be delivered during the second half of 2021.

THUNDERFISH® AUTONOMOUS UNDERWATER VEHICLE (AUV)

Kraken continues its ThunderFish® AUV development program. Kraken's original ThunderFish® AUV prototype is a technical upgrade of Fraunhofer's DeDave AUV. Kraken will pay Fraunhofer a royalty based on a percentage of each sale with minimum commitments starting in 2022. The ThunderFish® AUV was designed for deep sea military, commercial and scientific applications for use as a sensor and robotics technology demonstration platform to support ongoing development of the Company's underwater sensor and robotics programs.

Kraken has established a long-term technical co-operation program with Fraunhofer for technologies that can be deployed in Kraken's ThunderFish® AUV program. While Kraken is committed to grant research and development projects to Fraunhofer of €300,000 per year for a period of three years (2019-2021), these projects will be awarded to Fraunhofer as various statement of works are agreed upon and purchase orders issued. The remaining commitment under this program is €300,000. These projects will be expensed as incurred.

As a result of funding included in Kraken's OceanVision project, in Q3 2020 Kraken kicked off development of a ThunderFish® XL.

Building from the previous development efforts of the ThunderFish® Alpha AUV, the ThunderFish® XL AUV is being designed to be larger with an increased depth rating, larger payload capacity and longer mission endurance. It is being developed with the following key capabilities:

1. The ability to transition from high-speed survey mode to "zero" speed hovering mode in-mission;
2. Through-the sensor acoustic, laser and optical target detection, image recognition and inspection; and,
3. Using onboard sensors to improve vehicle navigational accuracy.

In the AUV space, Kraken is focused on using the ThunderFish® XL AUVs and procured AUVs to build a fleet of vehicles capable of providing Robotics as a Service rather than having a primary focus on selling AUVs. We expect that this will provide Kraken with a unique and valuable market position. The ThunderFish® XL AUV is expected to be in service in 2022 with R&D costs (excluding monies paid to Fraunhofer) being part of the OceanVision™ project.

AUTONOMOUS LAUNCH AND RECOVERY SYSTEMS (ALARS)

Launch and recovery of equipment offshore is one of the most dangerous phases of any ROV or AUV operation. Through the hiring of former Rolls Royce Marine employees in 2016, Kraken's Handling Systems Division has an experienced LARS engineering team with a proven track record. This group is developing both an intelligent winch system (TENTACLE™ and an autonomous LARS system that can launch AUVs from vessels, host facilities and docking stations. This group's capabilities are integral to various customer opportunities that Kraken is involved in or pursuing.

During 2020, as part of the OceanVision™ project, Kraken completed successful sea testing of the Kraken's ALARS, Tentacle Winch® and the KATFISH™ towed Synthetic Aperture Sonar underwater vehicle. Both the Tentacle Winch® and the ALARS are constructed of non-welded aluminum for high strength, low weight, and low magnetic signature.

KRAKEN POWER GMBH

Effective December 31, 2019, Kraken owns a 100% of Kraken Power GmbH. Kraken Power GmbH designs and manufactures unique pressure tolerant thrusters, drives, batteries, battery management systems, and electronics. These are specialized deep-sea components for AUVs and ROVs. Kraken Power's unique pressure tolerant gel encapsulation technology for lithium polymer batteries provides an attractively priced, eco-friendly and superior alternative to oil compensated batteries currently used for subsea battery applications. Kraken Power's technology and products enable a significant reduction in bill of material costs for our ThunderFish® AUV over acquiring conventional batteries.

On December 31, 2019 Kraken acquired the remaining 25% of Kraken Power not currently owned for €350,000, consisting of €250,000 in cash and the issuance of 236,258 common shares of the Company at \$0.62 per share. The transaction triggered

a change of control payment to an arm's length third-party lender to Kraken Power in an amount equal to €120,000 which was paid in Q3 2020. The purchase price has been reflected in the Statement of Changes in Shareholders' Equity while the change in control payment was recognized on the income statement in Q4 2019.

During Q1 2021, Kraken Power delivered its third order of batteries to a military customer.

ACOUSTIC SIGNAL PROCESSING GROUP (ASPG)

Kraken's Acoustic Signal Processing Group (ASPG) was established in mid 2018 and its employees have 80+ years of combined experience in sonar systems development and integration. Their core competency is implementation of digital signal processing and user interface software for Anti-Submarine Warfare (ASW) sonar applications. This work frequently involves integration with embedded processing platforms for shipboard or shore-based analysis systems. The group can process and display data from fixed and mobile underwater as well as airborne systems to take advantage of machine automation, active and passive array technology improvements, hardware and software upgrades of submarine, surface and airborne ASW systems.

ROBOTICS AS A SERVICE (RaaS)

Kraken believes that certain customers would prefer to hire the company to provide product output (i.e. imaging and bathymetry data) to them using the Kraken's own equipment, rather than the customer buying the equipment and having to own and operate and maintain the equipment. This is the genesis of Kraken's RaaS offering. Kraken expects RaaS to become a growing part of its revenue mix over time. Kraken will provide RaaS services to customers using Kraken's KATFISH™ towed underwater vehicles and AUVs such as ThunderFish® XL and Dive-LD and innovative sensors like the SeaVision® 3D laser system. While RaaS revenue is starting from a small base, Kraken is bidding on opportunities involving both shallow and deeper water surveys with the KATFISH™, ThunderFish®, and Dive-LD as well as our SeaVision® 3D laser system.

OCEANVISION™ PROJECT

The Company's OceanVision™ project is focused on the development of a RaaS offering for underwater seabed imagery and mapping. The OceanVision™ project began in the second half of 2019, with the contract formally signed in January 2020. OceanVision™ is a three-year, \$18.8 million project focused on the development of new marine technologies and products to enable an underwater robotics data acquisition and data analytics as a service business. This will be a turnkey service solution for ultra-high definition seafloor imaging, mapping and analytics, including simultaneous acquisition of ocean environmental and marine habitat data. It will result in an end-to-end digitalization solution offering advanced sensors, robots and data analytics as a turnkey service solution for seafloor imaging and mapping. Rapid high-throughput data analytics will make it possible to significantly reduce the cost of obtaining high resolution seafloor imaging and mapping allowing end-users to make more informed operational decisions in real-time.

The new technologies Kraken will develop within the scope of the OceanVision™ project are currently unavailable in a fully matured and tightly integrated offering in the commercial industry. The combination of a hovering-capable AUV with the potential for subsea residency, and a cutting-edge suite of acoustic and optical sensors, is a powerful package. As Kraken is the manufacturer of all the major vehicle components (i.e., sensors, batteries, propulsion system and software), it is Kraken's belief that its robotics platforms and services can be provided at a much lower overall cost than competing systems.

The project began in Q3 2019 and Kraken has deployed its sensors and unmanned underwater platforms to conduct ultra-high-definition seabed imaging and mapping on the Grand Banks of Newfoundland and other areas of Atlantic Canada as part of the OceanVision™ project. To date, Kraken has completed three offshore campaigns under this project.

To fund the OceanVision project, Canada's Ocean Supercluster will provide an investment of \$6.3 million, while the balance of the project of \$12.5 million will be provided by government agencies, industry partners (Petroleum Research Newfoundland and Labrador, Ocean Choice International, Nunavut Fisheries Association and NSP Maritime Link Incorporated) and Kraken. Kraken's commitment to the project is \$4.4 million, of which \$2.1 million remains outstanding at March 31, 2021. Kraken's commitment will be reduced if and when additional government and industry partners join the project in the future.

FINANCIAL CONTRIBUTIONS AWARDED

At March 31, 2021, Kraken had \$2.3 million remaining in grant funding to be drawn down against research and development activities. This excludes the remaining \$5.8 million of funding to be received under the OceanVision™ project.

Significant components of this remaining funding are as follows:

In August 2019, the Company was awarded funding for the development of a mooring chain laser inspection sensor for use in offshore oil and gas applications. Under the project, a total of \$1.8 million in funding is being provided in cash and in-kind services from Husky (\$1.26M) and the Government of Newfoundland and Labrador, through the Innovation and Business Investment Corporation (\$540,000). The project cash component received by Kraken will be \$720,000, of which \$558,673 has been received.

In August 2020, the Company was awarded \$2.9 million funding from the National Research Council of Canada Industrial Research Assistance Program (NRC IRAP). This funding is being used to support research and development of Kraken's Thunderfish® XL Autonomous Underwater Vehicle (AUV) and is also part of Kraken's OceanVision™ project of which \$912,989 has been received.

RESULTS OF OPERATIONS

Selected Annual Information

	Year Ended December 31, 2020 (\$)	Year Ended December 31, 2019 (\$)	Year Ended December 31, 2018 (\$)
Statement of Comprehensive Loss			
Total Revenues	12,274,899	15,145,976	6,707,956
Cost of Sales	6,452,048	8,441,506	3,902,538
Loss from operating activities	(4,773,250)	(3,177,038)	(3,982,668)
Net loss	(5,534,933)	(3,003,486)	(2,852,389)
Basic and diluted loss per share	(0.04)	(0.02)	(0.03)

	Year Ended December 31, 2020 (\$)	Year Ended December 31, 2019 (\$)	Year Ended December 31, 2018 (\$)
Statement of Financial Position			
Total Assets	34,820,074	18,090,876	14,028,465
Total Current Assets	25,644,350	13,498,657	9,738,966
Total Current Liabilities	14,696,183	6,262,178	4,815,590
Total Liabilities	18,808,651	8,427,558	5,731,030
Total Shareholders' Equity	16,011,423	9,663,318	8,297,435

The Company incurred a loss of \$5,534,933 for the year ended December 31, 2020, as compared with a loss of \$3,003,486 for the year ended December 31, 2019. Share-based payments of \$975,299 (2019 - \$1,370,745) were recorded upon the grant of incentive stock options pursuant to the Company's incentive stock option plan.

No cash dividends have been declared or paid since the date of incorporation and the Company has no present intention of paying dividends on its common shares. The Company anticipates that all available funds will be used to finance the growth of its business.

Summary of Quarterly Information

Selected financial information for each of the eight most recently completed quarters are as follows:

	Revenue (\$)	Operating activity less share based payments (\$)	Share-based payments (\$)	Net income (loss) (\$)	Comprehensive income (loss) \$	Basic and diluted income (loss) per share (\$)
Q1 2021	3,601,204	2,394,616	117,655	(604,356)	(689,056)	(0.00)
Q4 2020	2,056,832	3,902,994	107,202	(3,530,650)	(3,538,232)	(0.02)
Q3 2020	1,545,463	2,796,150	412,319	(2,603,496)	(2,593,227)	(0.02)
Q2 2020	2,281,929	1,689,057	220,420	(128,724)	(165,953)	0.00
Q1 2020	6,390,675	1,882,739	235,358	727,937	1,005,882	0.00
Q4 2019	4,616,644	2,114,536	288,276	(237,546)	(634,081)	0.00
Q3 2019	7,822,452	2,585,027	999,469	95,242	317,253	0.00
Q2 2019	1,337,495	2,486,264	8,200	(1,988,914)	(1,944,881)	(0.01)

Note: Operating expenses are defined as administrative expenses, R&D costs and depreciation and amortization.

Comparative balance sheet information for 2020 and 2019 is presented below:

	Total Assets (\$)	Total Current Assets (\$)	Total Current Liabilities (\$)	Total Liabilities (\$)
Q1 2021	32,037,380	22,730,024	12,199,159	16,445,491
Q4 2020	34,820,074	25,644,350	14,696,183	18,808,651
Q3 2020	16,522,469	11,427,782	4,644,690	7,073,870
Q2 2020	19,136,681	14,166,234	5,320,246	7,707,041
Q1 2020	19,248,329	14,224,596	5,983,912	8,293,155
Q4 2019	18,090,876	13,498,657	6,262,178	8,427,558
Q3 2019	17,273,370	12,492,410	4,776,548	7,116,466
Q2 2019	20,090,135	13,892,388	8,867,266	11,164,027

Three Months Ended March 31, 2021

The Company recorded revenues of \$3,601,204 (2020 - \$6,390,675) from progress revenue from the Danish Navy contract as well as the sale of subsea batteries, decrease of 44% compared to the same period a year ago. Prior year revenue was driven by the delivery of a KATFISH™, subsea batteries, the provision of software services and survey support work. The Company's revenue can fluctuate significantly on a quarterly basis mainly due to the timing of orders, progress towards completion and lead times on parts purchases. At March 31, 2021, the Company had contract liabilities of \$7,628,217 (December 31, 2020 - \$8,761,477), which represent customer advances on product orders.

Cost of sales were lower than that of the prior year at \$1,450,862 (2020 - \$3,472,702). The decrease in cost of sales was due to the cost associated with the manufacturing of a KATFISH™, subsea batteries and labour associated with providing service revenue in the prior year. The Company realized gross profit of \$2,150,342 (2020 - \$2,917,973). Gross margin for the quarter was 60%, as compared to 46% gross margin in the prior first quarter.

Administrative expenses in the quarter increased 7% to \$1,633,157 compared to \$1,520,759 in the prior year due to both an increase in headcount and various administrative expenses such as rent and software subscriptions. At the end of March 31, 2021, Kraken employed 149 employees compared to 108 in the prior year. Other notable items in the Administrative expense category include Accounting and legal \$82,595 (2020 - \$98,516) travel related costs of \$13,511 (2020 - \$89,798), which decreased due to COVID related cancellations for business meetings, trade shows and conferences. Also included were rent of \$80,172 (2020 - \$61,384), consulting fees of \$67,640 (2000- \$12,507) and software subscriptions \$171,130

(2020 - \$128,451) due to the implementation of a new ERP system. During the quarter, the Company realized a foreign exchange loss of \$2,984 (2020 foreign exchange loss - \$54,825).

Depreciation in the quarter totalled \$304,489 (2020 - \$185,462) and increased due to a higher property and equipment base. Amortization of intangible assets increased to \$75,872 (2020- \$72,357) due to changes in foreign exchange rate movements.

Research and development costs (“R&D”) in the quarter increased to \$381,098 (2020 - \$104,161), as a result of the timing of expenditures on various R&D programs as well as the timing of government assistance and reimbursements from the Ocean SuperCluster/funding partners which are netted against R&D.

During the three months ended March 31, 2021, the Company received government assistance, excluding the OceanVision project, in the amount of \$855,026 (2020 - \$868,955). Government Assistance has been classified as a reduction to Cost of Sales \$68,271 (2019 - \$Nil), Research & Development expense \$682,555 (2020 – \$667,561) and Administrative expense \$104,200 (2020 - \$Nil).

The financial statements reflect a cost reimbursement under Kraken’s OceanVision project, including \$535,729 (2020 - \$618,462) in reimbursements from the Ocean SuperCluster and \$247,485 (2020 - \$230,081) in reimbursements by funding partners. Assistance related to the OceanVision project has been classified as a reduction to Research & Development expense of \$449,482 (2020 – \$314,903), Administrative expense \$25,625 (2020 – \$12,893), Cost of sales \$Nil (2020 – \$14,352) and Construction in progress of \$308,107 (2020 - \$506,395).

Share-based compensation of \$117,655 was recorded, representing the fair value of the options that vested during the three months ended March 31, 2021. During the same period of the prior year, the Company recorded share-based compensation of \$235,358. The decrease over the prior year is a result of reduced options granted in 2020.

The Company recorded net loss of \$604,356 and comprehensive loss of \$689,056 for the quarter, as compared to a net income of \$727,937 and comprehensive income of \$1,005,882 for the same period of prior year.

LIQUIDITY AND CAPITAL RESOURCES

At March 31, 2021, the Company had working capital of \$10,530,865 (December 31, 2020 – \$10,948,167). Cash and cash equivalents as at March 31, 2021 was \$9,004,024, as compared with \$12,924,509 at December 31, 2020. In addition, the Company had restricted cash of \$1,045,502 (December 31, 2020 - \$1,057,982) held in a Guaranteed Investment Certificate as security for letters of credit for advance payments received under a manufacturing contract and mature October 30, 2023.

During the three months ended March 31, 2021, the Company received proceeds of \$151,867 (March 31, 2020 - \$50,616) upon the exercise of 698,334 stock options. During the three months ended March 31, 2021, the Company experienced cash outflows of \$3,492,411 (2020 – inflow of \$359,651) from operating activities. Cash outflows from investing activities were \$679,545 versus \$402,974 for 2020. Financing activities realized inflows of \$301,027 (2020 – outflow of \$39,793) and included proceeds of \$151,867 received upon option exercises.

Overall, excluding the foreign exchange impact on cash, cash decreased by 3,870,929 as compared to a decrease of \$83,116 during the prior year.

RISKS AND UNCERTAINTIES

The Company is a relatively new company with limited operating history and, in addition to facing all of the competitive risks in the underwater sonar and robotics sector it will face all the risks inherent in developing a business including: access to capital, ability to attract and retain qualified employees, ability to attract and maintain customers and the ability to put in place appropriate operating and control procedures.

Industry specific risks include, but are not limited to:

- *Competitive risk* – the sonar industry in which the Company operates is highly competitive. The competitors of the Company range from small single product companies to diversified corporations in the military, sonar and marine imaging industry. Some of the competitors of the Company may have more extensive or more specialized engineering, manufacturing, and marketing capabilities;

- *Technology risk* – The future success of the Company will depend on its ability to develop new technologies that achieve market acceptance. The sonar market is characterized by rapidly-changing technologies and evolving industry standards;
- *Protection of Intellectual Property*: The Company may be unable to adequately protect its intellectual property rights, which could affect its ability to compete. Protecting the Company’s intellectual property rights is critical to its ability to compete and succeed as a company. The Company currently has trademark registrations and relies on a combination of copyright, trademark, and trade secret laws, confidentiality procedures, contractual provisions and other measures to protect its proprietary information. However, all of these measures afford only limited protection;
- *Outside suppliers*: The Company’s operations depend on component availability and the manufacture and delivery by key suppliers of certain products and services. Further, the Company’s operations are dependent on the timely delivery of materials by outside suppliers. The Company cannot be sure that materials, components, and subsystems will be available in the quantities required, if at all;
- *Government contracts*: The Company will depend, in part, on government contracts, which may only be partially funded, subject to termination, heavily regulated, and audited. The termination of one or more of these contracts could have a negative impact on the operations of the Company; and
- *Competitive bidding*: The Company will derive significant revenue from contracts awarded through a competitive bidding process, which can impose substantial costs upon it, and the Company could fail to maintain its current and projected revenue if it fails to compete effectively.

An investment in the Company’s common shares is highly speculative and subject to a number of risks and uncertainties. Only those persons who can bear the risk of the entire loss of their investment should participate. An investor should carefully consider the risks described above and the other information filed with the Canadian securities regulators before investing in the Company’s common shares. The risks described above are not the only ones faced. Additional risks that the Company currently believes are immaterial may become important factors that affect the Company’s business. If any of these risks occur, or if others occur, the Company’s business, operating results and financial condition could be seriously harmed and investors may lose all of their investment.

CAPITAL MANAGEMENT

The Company’s objectives when managing its capital are to maintain a financial position suitable for supporting its operations and growth strategies, to provide an adequate return to shareholders and to meet its current obligations.

The Company’s capital structure consists of shareholders’ equity and long-term note payable. The Company makes adjustments to the capital structure depending on economic conditions, its financial position and performance. In order to maintain or adjust the capital structure, the Company may issue new shares, buyback shares or pay dividends, issue new debt and sell assets to reduce debt.

FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

As at March 31, 2021, the Company’s risk exposures and the impact of the Company’s financial instruments are summarized below:

Credit Risk:

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was:

	March 31, 2021	December 31, 2020
Cash and cash equivalents and restricted cash	\$ 10,049,526	\$ 13,982,491
Trade and other receivables	2,618,267	3,119,920
	\$ 12,667,793	\$ 17,102,411

At March 31, 2021, 71% of the trade receivables balance was owing from 2 customers (2020 – 69% of the trade receivables was owing from 2 customers). At March 31, 2021, the Company had recorded contract liabilities of \$7,628,217 (2020– \$8,761,477).

Liquidity Risk:

Liquidity risk is the risk that the Company will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Company’s approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions. As of March 31, 2021, the Company had a cash balance of \$9,004,024 (December 31, 2020 - \$12,924,509) to settle current liabilities of \$12,350,913 (December 31, 2020 - \$14,696,183) of which contract liabilities make up \$7,628,217 (December 31, 2020 - \$8,761,477). The company has an operating line of credit to cover short-term liquidity needs in the amount of \$1,500,000 and €500,000, at March 31, 2021 the company had \$1,500,000 and €34,258 available.

Market Risk:

Market risk is the risk of loss that may arise from changes in market factors such as interest rates, foreign exchange rates, and commodity and equity prices.

(a) Interest rate risk

At March 31, 2021, the Company held \$9,004,024 in cash and cash equivalents, \$1,045,502 in restricted cash and has drawn \$688,259 against its operating line of credit. The drawn operating line of credit bears interest annually at 3.95%, payable monthly.

(b) Foreign currency risk

The Company’s exposure to foreign currency risk is limited to sales, certain purchases, short-term and long-term obligations in USD, EUR, GBP and DKK. The Company does not use any form of hedging against fluctuations in foreign exchange.

Fair Value:

During the three months ended March 31, 2020, there were no transfers between level 1, level 2 and level 3 classified assets and liabilities. The following table presents the fair value and fair value hierarchy of the Company’s financial instruments and excludes financial instruments measured at amortized cost that are short-term in nature. The carrying values of the Company’s financial instruments approximate their fair values except for long-term debt:

March 31, 2021	Level 1	Level 2	Level 3
Financial liabilities at amortized cost:			
Long-term note payable		988,327	-
December 31, 2020	Level 1	Level 2	Level 3
Financial liabilities at amortized cost:			
Long-term note payable	-	668,860	-

USE OF ESTIMATES AND JUDGMENTS

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates. Estimates are reviewed on an ongoing basis based on historical experience and other factors that are considered to be relevant under the circumstances. Revisions to estimates on the resulting effects of the carrying amounts of the Company’s assets and liabilities are accounted for prospectively.

All of the Company's significant accounting policies and estimates and judgments are included in Notes 2,3 and 4 of its audited consolidated financial statements for the year ended December 31, 2020, as well as Note 2 to the interim financial statements.

SUBSEQUENT EVENTS

Subsequent to March 31, 2021, the Company:

- (a) 83,333 options were exercised for proceeds of \$20,833.
- (b) On April 7, 2021, Kraken filed a short form base shelf prospectus with securities regulators in each of the provinces and territories of Canada, which will qualify the distribution of up to \$65 million of common shares, warrants, subscription receipts, and debt securities.
- (c) On April 8, 2021, Kraken announced that it had signed a non-binding letter of intent to acquire subsea services company, PanGeo Subsea Inc.
- (d) On April 19, 2021, Kraken announced that it had acquired 13 Robotics Ltda of Brazil for US\$220,000. At this time the purchase price allocation has not been determined due to how recent the acquisition has closed.

OUTSTANDING SHARE DATA AS AT May 26, 2020:

- (a) Authorized and issued share capital:

Class	Par Value	Authorized	Issued Number
Common	No par value	Unlimited	168,599,020

- (b) Summary of options outstanding:

Security	Number	Number Exercisable	Exercise Price	Expiry Date
Options	525,000	525,000	0.25	July 18, 2021
Options	500,000	500,000	0.70	March 5, 2022
Options	1,500,000	1,000,000	0.63	July 14, 2022
Options	400,000	400,000	0.63	July 14, 2022
Options	2,656,666	1,738,384	0.53	September 8, 2022
Options	75,000	50,000	0.44	May 1, 2023
Options	1,500,000	500,000	0.57	July 14, 2023
Options	300,000	100,000	0.51	August 5, 2023
Options	1,000,000	500,000	0.63	July 14, 2024
	8,456,666	5,313,384		

DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

Disclosure controls and procedures ("DC&P") are intended to provide reasonable assurance that material information is gathered and reported to senior management to permit timely decisions regarding public disclosure. Internal controls over financial reporting ("ICFR") are intended to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with IFRS accounting principles.

TSX Venture-listed companies are not required to provide representations in their annual and interim filings relating to the establishment and maintenance of DC&P and ICFR, as defined in Multinational Instrument MI 52-109. In particular, the CEO and CFO certifying officers do not make any representations relating to the establishment and maintenance of (a) controls and other procedures designed to provide reasonable assurance that information required to be disclosed by the issuer in its annual filings, interim filings or other reports filed or submitted under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation, and (b) processes to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with the issuer's GAAP.

OTHER INFORMATION

Additional information regarding the Company is available on SEDAR at www.sedar.com and on the Company's website at www.krakenrobotics.com.